

Curt Pringle, Chairman  
Tom Umberg, Vice-Chair  
Russell Burns  
David Crane  
Rod Diridon, Sr.\*  
Fran Florez\*  
Richard Katz  
Judge Quentin L. Kopp\*  
Lynn Schenk  
\*past chair

ARNOLD SCHWARZENEGGER  
GOVERNOR



## CALIFORNIA HIGH-SPEED RAIL AUTHORITY

April 19, 2010

Elaine M. Howle  
State Auditor  
Bureau of State Audits  
555 Capitol Mall, Suite 300  
Sacramento, CA 95814

Dear Ms. Howle:

Thank you for the opportunity to review and comment on the draft audit report regarding the California High-Speed Rail Authority (Authority).

The Authority is committed to transparency and believes strongly that additional spotlight on our operations will ultimately make for a better high-speed train project for the state. So, the Authority appreciates the input and recommendations from the Bureau of State Audits, and agrees with its recommendations.

We believe the audit process has identified areas where the Authority can improve its administrative processes and project oversight. We note that many of the findings in your draft audit are similar to those outlined earlier by the Legislative Analyst's Office (LAO). As a result, in many instances the Authority has already taken action to address issues raised in your report. In particular, the Authority earlier this month approved an addendum to its 2009 Business Plan that clarified our efforts to address funding for system construction, risk management, and alternatives for securing the private capital investments necessary to bring this important project to fruition. We appreciate that in many cases the draft audit takes note that the Authority is already taking steps to improve its operations based on recommendations made earlier by the LAO, as well as on findings in your draft audit.

We do believe, however, that the report's inflammatory title is overly aggressive considering that the contents of the audit's findings are not equally scathing. While the Authority is appreciative that the report in its entirety reflects more objectively the challenges of a state entity in transition from a planning body to one responsible for implementing a large-scale public infrastructure project, we also appreciate that not all Californians are able to read each and every word in the audit report and therefore may be misled by the title and headlines contained within.

The audit report's detail correctly describes the enormity and complexity of the high-speed train project. It also correctly describes the organizational structure of the Authority and the

Elaine M. Howle  
April 19, 2010

recent budget changes that have occurred to supplement staffing. It's important to note that staffing levels have been a concern of the Authority Board for some time, and which it has therefore taken significant action to address. This includes contracting out for an organizational assessment and working quickly to hire a chief executive officer.

This is a historic project for California, which has the potential to bring tens of thousands of jobs to the state in the near term and bring improved mobility, increased economic strength, and environmental benefits in the long-term. The Authority is committed to building the high-speed train system in a responsible way that reflects the will of the people of the state, and in that task, we are grateful for the partnership and additional oversight of entities such as the Bureau of State Audits.

Our response to the draft audit report follows the recommendations presented at the end of the report. Our responses are contained in the attached document.

With appreciation,

A handwritten signature in blue ink, appearing to read "Curt Pringle". The signature is stylized and cursive.

Curt Pringle, Chairman  
California High-Speed Rail Authority

Attachment

## Attachment

### General Response

- The Authority is committed to transparency and believes strongly that additional spotlight on our operations will ultimately make for a better high-speed train project for the state. The Authority appreciates the input and recommendations from the Bureau of State Audits, and agrees with its recommendations.
- We believe the audit process has identified areas where the Authority can improve its administrative processes and project oversight. We appreciate that in many cases the draft audit takes note that the Authority is already taking steps to improve its operations based on recommendations made earlier by the LAO, as well as on findings in your draft audit.
- We do believe, however, that the report's inflammatory title is overly aggressive considering that the contents of the audit's findings are not equally scathing.
- The draft audit report correctly describes the enormity and complexity of the high-speed train project. It also correctly describes the organizational structure of the Authority and the recent budget changes that have occurred to supplement staffing.
- This is a historic project for California, which has the potential to bring tens of thousands of jobs to the state in the near term and bring improved mobility, increased economic strength, and environmental benefits in the long-term. The Authority is committed to building the high-speed train system in a responsible way that reflects the will of the people of the state.

### BSA Recommendations and Authority Responses

*Recommendation: The Authority should develop and publish alternative funding scenarios that reflect the possibility of reduced or delayed funding from planned sources ... should detail the implications of variations in the level or timing of funding for the program and its schedule.*

**Response:** The Authority agrees that it is important to be aware and plan for funding scenarios that differ from the scenario we feel is most likely and have therefore presented those in our December 2009 Report to the Legislature. It is important to note that alternate scenarios would not vary in terms of the ratio of state to federal to private funding. Instead, alternate scenarios would be presented as lengthened timelines for construction and for bringing online revenue-based passenger service, which in turn would mean an increased project cost as inflation affects the cost of materials and labor.

*Recommendation: Authority should further specify the potential cost of revenue guarantees and who would pay for them.*

Elaine M. Howle  
April 19, 2010

Response: The Authority agrees that, as we move from the environmental planning phase to an implementation phase, it will be important to further detail the concept of a minimum revenue guarantee, its cost and the entity we would propose to be responsible for such a guarantee. The Authority has already asked its financial consultant to address these issues within the context of the overall proposed procurement and risk-transfer strategy, which is scheduled to commence with a Request for Qualifications process late this year and with a Request for Proposals process in 2011. Additionally, we have been working with our legal counsel on this issue and will ask for a written opinion on the matter prior to bringing such a proposal before the Legislature.

Recommendation: *Authority should assure that it implements planned actions related to managing risk.*

Response: The Authority agrees that risk management is a top priority. Your report correctly notes that, to that end, the Authority in February 2010 hired a risk insurance manager, and that in March 2010 the Program Management Team revised its risk and mitigation development protocol. Additionally, in 2009, the Authority contracted for an independent organizational assessment, which was conducted by the firm KPMG. This assessment recommended an organizational structure that includes an office for "Project Controls & Risk Management," which would report directly to the Authority's chief executive officer. The Authority in November 2009 approved the recommended organizational chart and has been working, within the state hiring process, toward putting the staffing plan in place. One element of that is establishing an auditing office, which is an element of the Authority's 2010-11 annual budget request.

Recommendation: *Authority should ensure that the review group adheres to the Meeting Act of seek a formal opinion from the Office of the Attorney General regarding whether the review group is subject to this act.*

Response: The report correctly states that the Authority has received legal advice suggesting that the Independent Peer Review Group was not intended to be set up as a public entity operating within the structure required by Bagley-Keene. But we agree that this is a topic that merits clarity. To that end, the Authority will continue to work on this issue with its lead legal counsel (a deputy attorney general from the Office of the Attorney General). Additionally, the Authority will approach the Legislature with the Bureau of State Audits' question pertaining to its intent, in that the Independent Peer Review Group is a legislatively created entity. The Authority welcomes working with the Peer Review Group, and respects its independence.

Recommendation: *Authority should track expenditures for [administrative and preconstruction] activities and develop a long-term spending plan for them. It should also develop procedures and systems to ensure it complies with Recovery Act requirements.*

Elaine M. Howle  
April 19, 2010

Response: The Authority thanks the Bureau of State Audits for its recommendation to develop a long-term spending plan for preconstruction activities and will do so. The Authority has already begun to bring online a database for tracking expenditures, which will include detailed provisions for monitoring expenditures by source and mechanisms to alert staff to potential problems. This database system is scheduled to be in place in May 2010. Regarding the Recovery Act, the Authority has already reached out to and begun working in cooperation with the Governor's Recovery Act Task Force, and will review all Recovery Act requirements and implement procedures to track compliance.

Recommendation: *Should amend the program management oversight consultant's work plan to include a critical review of progress reports for accuracy and consistency. Authority staff should also assure that the Program Manager revises its progress reports to include information on the status of promised products and services.*

Response: We agree that critical review of the Program Manager's monthly progress reports should be included within the Program Management Oversight consultant's scope of work. In fact, we already believed the consultant's scope of work to be inclusive of this task, and the Program Management Oversight consultant is already engaged in the process of reviewing and assisting the Program Manager in revamping these important reports. Additionally, the reports have been the subject of two public meetings before the Authority's Operations Committee, the result of which is that a new reporting procedure has been put in place by the Board Committee. To provide greater clarity that this task is already underway and is a part of the Program Management Oversight team's scope of work, the Authority will explore explicitly calling out in writing this element of the consultant's work.

Recommendation: *Should ensure that staff adhere to controls for processing invoices ... should not pay invoices from regional contractors until they receive notification from the Program Manager that the work billed has been performed, or until they have conducted an independent verification.*

Response: The Authority thanks the Bureau of State Audits for identifying this weakness in our protocols. While this verification and notification has indeed been occurring, it has often been informal and/or verbal. And though no improprieties have occurred as a result of the current process, the Authority agrees that this is a process that must be improved by being documented in writing. The Authority will formalize this process such that verification and notification is made routinely in written and therefore easily documented form.

Recommendation: *Authority should adhere to the conditions of its contracts and work plans, and make any amendments or modifications to work plans in writing.*

Response: The Authority agrees and will review all contracts and work plans to identify any that require modifications or amendments. Additionally, it should be noted that in January 2010, the Authority brought aboard a state employee assigned as contract

Elaine M. Howle  
April 19, 2010

manager to the Authority's regional engineering consultants with the responsibility to audit, oversee, and correct instances such as those described in the report.

*Recommendation: Authority should participate in the development of key policy documents, such as the Authority's business and strategic plans. Further, Authority members should adhere to their policies and procedures, including those outlining how they may communicate with contractors.*

**Response:** The Authority strongly agrees and appreciates that the Bureau of State Audits recognized in its report the Authority's increased participation in the project's development and details over the past eight months. The report notes that Board members were involved in the development of the strategic plan and the business plan, but that involvement has already increased, with the Board Executive/Administrative Committee giving significant input into the strategic plan during an April 7 public meeting and the entire Board reviewing and unanimously approving an addendum to the business plan at an April 8 meeting. Additionally, in light of this draft audit report, the Board has been re-advised on its approved method for communicating with contractors, which is one subject of a revision/addition to the Authority's Board Policies & Procedures, which was discussed April 7 in a Board Committee meeting and will be brought back to a May or June Board meeting.

*Recommendation: Authority should ensure its written policies and procedures reflect intended controls over invoice processing and offer sufficient detail to guide staff. These procedures should include steps for documenting implementation of invoice controls.*

**Response:** The Authority will review its contract administration manual and will identify areas, such as controls over invoice processing, to make certain that policies and procedures are adequately detailed in a manner that ensures effective controls are in place. For deficient or missing policies, staff will prepare them and communicate them to staff responsible for invoice payments.